



## THE LOTOS GROUP

### MANAGEMENT'S DISCUSSION AND ANALYSIS OF THE FINANCIAL PERFORMANCE IN Q3 2011

*This is a translation of a document originally issued in Polish.*

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## 1 Market environment

**Table 1: Macroeconomic data**

|   |         | Q3<br>2011 | Q2<br>2011 | Q3<br>2010 | Q3 2011<br>vs.<br>Q2 2011 | Q3 2011<br>vs.<br>Q3 2010 |
|---|---------|------------|------------|------------|---------------------------|---------------------------|
| DATED Brent FOB prices                  | USD/bbl | 113.41     | 117.04     | 76.86      | -3.1%                     | 47.6%                     |
| Urals CIF Rotterdam prices              | USD/bbl | 111.52     | 113.73     | 75.58      | -1.9%                     | 47.6%                     |
| Brent/Urals differential *              | USD/bbl | 0.75       | 2.86       | 0.92       | -73.8%                    | -18.5%                    |
| Model refining margin USD/bbl**         | USD/bbl | 2.34       | 2.92       | 3.3***     | -19.9%                    | -29.1%                    |
| Crack margin: Gasoline                  | USD/t   | 166.56     | 172.21     | 119.55     | -3.3%                     | 39.3%                     |
| Crack margin: Diesel oil (10 ppm)       | USD/t   | 110.49     | 100.16     | 91.19      | 10.3%                     | 21.2%                     |
| Crack margin: Light fuel oil            | USD/t   | 85.81      | 73.43      | 70.74      | 16.9%                     | 21.3%                     |
| Crack margin: Aviation fuel             | USD/t   | 158.79     | 168.11     | 115.89     | -5.5%                     | 37.0%                     |
| Crack margin: Heavy fuel oil            | USD/t   | -231.07    | -264.45    | -158.28    | 12.6%                     | -46.0%                    |
| Dollar exchange rate at end of period   | PLN/USD | 3.26       | 2.75       | 2.93       | 18.5%                     | 11.3%                     |
| Euro exchange rate at end of period     | PLN/EUR | 4.41       | 3.99       | 3.99       | 10.5%                     | 10.5%                     |
| Average quarterly PLN/USD exchange rate | PLN/USD | 2.94       | 2.75       | 3.10       | 6.9%                      | -5.2%                     |
| Average quarterly PLN/EUR exchange rate | PLN/EUR | 4.15       | 3.96       | 4.01       | 4.8%                      | 3.5%                      |

\* Brent vs. Urals spread.

\*\*Model margin for an output structure in an averaged scenario of typical annual operation of Grupa LOTOS S.A.'s refinery, assuming maximization of output of middle distillates. An annual throughput has been assumed that corresponds to the maximum distillation capacity if Urals crude was the only input (the value of Urals crude is determined as the difference between DTD Brent and the Urals Rtd vs. forward Dtd Brent spread).

\*\*\*The Q3 2010 figure given for the purpose of comparison. In Q3 2010, Grupa LOTOS S.A.'s refinery had a different technological configuration in connection with the ongoing 10+ Programme.

The most significant macroeconomic factors that had a material impact on the LOTOS Group's performance in Q3 2011 were higher crude oil prices and a drop in the average quarterly PLN/USD exchange rate relative to Q3 2010. Concurrently, the third quarter of 2011 saw a significant depreciation of the zloty, from PLN/USD 2.75 on June 30th 2011 to PLN/USD 3.26 on September 30th 2011.

In Q3 2011, the average quarterly price of Brent Dated crude was higher by 47.6% relative to the comparative period, i.e. Q3 2010. Relative to the previous quarter, i.e. Q2 2011, the price of Brent Dated fell by 3.1% and the Brent/Urals differential contracted strongly by 73.8%.

Relative to the same period of the previous year, Q3 2011 saw an improvement in crack margin on fuels and a decline in crack margin on heavy fuel oil. Compared with the previous quarter, i.e. Q2 2011, prices of diesel oil and light fuel oil increased in the analysed quarter.

**Strong depreciation  
of PLN vs. USD at  
the end of Q3 2011**

## 2 Upstream segment

**Table 2: Crude oil reserves, production and sales**

| Crude oil          |                |                |                |                     |                     |
|--------------------|----------------|----------------|----------------|---------------------|---------------------|
| Reserves (mmbbl) * | Sep 30 2011    | Jun 30 2011    | Sep 30 2010    |                     |                     |
| Norway             | 12.95          | 12.95          | 12.95          |                     |                     |
| Poland             | 34.17          | 34.45          | 35.27          |                     |                     |
| Lithuania **       | 6.63           | 6.79           | NA             |                     |                     |
| <b>total</b>       | <b>53.75</b>   | <b>54.19</b>   | <b>48.22</b>   |                     |                     |
| Production (bbl/d) | Q3 2011        | Q2 2011        | Q3 2010        | Q3 2011 vs. Q2 2011 | Q3 2011 vs. Q3 2010 |
| Poland             | 3,032          | 3,149          | 3,163          | -3.7%               | -4.1%               |
| Lithuania **       | 1,803          | 1,707          | NA             | 5.6%                | -                   |
| <b>total</b>       | <b>4,835</b>   | <b>4,856</b>   | <b>3163</b>    | <b>-0.43%</b>       | <b>52.86%</b>       |
| Sales (bbl)        | Q3 2011        | Q2 2011        | Q3 2010        | Q3 2011 vs. Q2 2011 | Q3 2011 vs. Q3 2010 |
| Poland             | 211,213        | 447,664        | 221,936        | -52.8%              | -4.8%               |
| Lithuania **       | 155,347        | 172,650        | NA             | -10.0%              | -                   |
| <b>total</b>       | <b>366,560</b> | <b>620,314</b> | <b>221,936</b> | <b>-40.9%</b>       | <b>65.2%</b>        |

\*2P – proved and probable reserves.

\*\* Based on the interest held in the AB Geonafta Group.

**Table 3: Natural gas reserves, production and sales**

| Natural gas            |             |             |             |                     |                     |
|------------------------|-------------|-------------|-------------|---------------------|---------------------|
| Reserves (bcm) as at * | Sep 30 2011 | Jun 30 2011 | Sep 30 2010 |                     |                     |
| Poland                 | 0.509       | 0.513       | 0.525       |                     |                     |
| Production (mcm)       | Q3 2011     | Q2 2011     | Q3 2010     | Q3 2011 vs. Q2 2011 | Q3 2011 vs. Q3 2010 |
| Poland                 | 4.0         | 3.8         | 4.1         | 6.4%                | -1.4%               |
| Sales (mcm)            | Q3 2011     | Q2 2011     | Q3 2010     | Q3 2011 vs. Q2 2011 | Q3 2011 vs. Q3 2010 |
| Poland                 | 2.5         | 2.2         | 2.4         | 13.6%               | 2.4%                |

\*2P – proved and probable reserves.

### Poland

In Q3 2011 in the Baltic Sea, production of oil and gas from the B3 field continued, and further analytical and designing work was under way in preparation for development of the B8 field. Furthermore, starting from July 20th 2011 the B8-Z5 injection well in the B8 field was being drilled. Preparations to launch temporary production from the B8 field.

### Lithuania

In Q3 2011, oil production from the Girkaliai, Kretinga, Nausodis and Genciu fields was conducted, the Lizai-2 appraisal/production well was drilled under a licence held by UAB

**Production from B3 field continuing in Q3 2011**

**Crude oil output in Lithuania at 1,803 bbl/d**

Manifoldas and drilling work started to spud the Genciu-14HR well in the Genciaj field (UAB Genciu).

### Norway

In Q3 2011, development work continued as part of the YME production project. According to the information obtained from Talisman Energy, production from the field is expected to be launched in the second quarter of 2012.

LOTOS E&P Norge AS, which is the operator of the PL503 and PL503B licences, completed the 3D seismic surveys and commenced processing of the seismic data.

Furthermore, as the operator of the PL498 licence, the company started preparations to drill the first exploration/appraisal well (in late Q2/early Q3 2012), as part of which in October 2011 it signed an agreement with Maersk Drilling. In Q3 2011, LOTOS E&P Norge AS continued preparations to drill (in Q2 2012) an exploration/appraisal well under the PL497 licence.

**Table 4: Operating results of the upstream segment**

|                               |             | Q3 2011 | Q2 2011 | Q3 2010 | Q3 2011<br>vs.<br>Q2 2011 | Q3 2011<br>vs.<br>Q3 2010 |
|-------------------------------|-------------|---------|---------|---------|---------------------------|---------------------------|
| Sales revenue                 | <i>PLNm</i> | 128.9   | 210.3   | 51.4    | -38.7%                    | 150.8%                    |
| Operating profit/(loss)       | <i>PLNm</i> | 43.5    | 84.3    | 6.1     | -48.4%                    | 613.1%                    |
| Depreciation and amortisation | <i>PLNm</i> | 27.6    | 25.4    | 14.8    | 8.7%                      | 86.5%                     |
| EBITDA                        | <i>PLNm</i> | 71.1    | 109.7   | 20.9    | -35.2%                    | 240.2%                    |

**Operating profit of  
the upstream  
segment at  
PLN 43.5m**

In Q3 2011, sales revenue of the upstream segment was PLN 77.5m higher than in Q3 2010, mainly due to the rise in oil prices and higher oil sales volumes following the acquisition of control (on February 3rd 2011) over AB Meditus, holder of a 59.41% interest in AB Geonafra. PLN 81.4m lower sales revenue in Q3 2011 than in Q2 2011 was attributable chiefly to lower volumes of the Rozewie crude sold due to the delivery schedule.

The segment's sales revenue for Q3 2011 includes PLN 62.8m of revenue of the AB Meditus Group. The volume of oil sales in Q3 2011 was 366.6 thousand bbl (47.2 thousand tonnes) and included 155.3 thousand bbl (20.0 thousand tonnes) of crude oil produced in the Lithuanian fields and sold outside the Group. The upstream segment's operating result includes PLN 21.1m of profit earned by companies of the AB Meditus Group.

### 3 Downstream segment

**Table 5: Structure of crude oil refining**

|  |             | Q3 2011 | Q2 2011 | Q3 2010 | Q3 2011<br>vs.<br>Q2 2011 | Q3 2011<br>vs.<br>Q3 2010 |
|--|-------------|---------|---------|---------|---------------------------|---------------------------|
| Volume of crude processed by the Gdańsk refinery | 000' tonnes | 2,359.7 | 2,220.0 | 2,196.2 | 6.3%                      | 7.4%                      |
| including:                                       |             |         |         |         |                           |                           |
| Urals crude                                      | 000' tonnes | 2,245.8 | 1,934.9 | 1,731.1 | 16.1%                     | 29.7%                     |
| Rozewie crude                                    | 000' tonnes | 51.8    | 28.7    | 41.8    | 80.5%                     | 23.9%                     |
| Other types of crude                             | 000' tonnes | 62.1    | 256.4   | 423.3   | -75.8%                    | -85.3%                    |

**Higher crude oil refining output in Q3 2011**

Higher volumes of crude oil processed in the analysed period is attributable to completion of the 10+ Programme and optimisation of production.

**Table 6: Structure of Grupa LOTOS S.A.'s production**

|                    |             | Q3 2011 | Q2 2011 | Q3 2010 | Q3 2011<br>vs.<br>Q2 2011 | Q3 2011<br>vs.<br>Q3 2010 |
|--------------------|-------------|---------|---------|---------|---------------------------|---------------------------|
| Total output       | 000' tonnes | 2,653.9 | 2,474.3 | 2,351.5 | 7.3%                      | 12.9%                     |
| Gasolines          | 000' tonnes | 372.3   | 342.8   | 366.9   | 8.6%                      | 1.5%                      |
| Raw gasoline       | 000' tonnes | 24.4    | 23.6    | 31.3    | 3.4%                      | -22.0%                    |
| Diesel oil         | 000' tonnes | 1,245.3 | 1,178.4 | 1,080.9 | 5.7%                      | 15.2%                     |
| Light fuel oil     | 000' tonnes | 81.4    | 64.3    | 77.0    | 26.6%                     | 5.7%                      |
| Aviation fuel      | 000' tonnes | 140.6   | 101.4   | 75.2    | 38.7%                     | 87.0%                     |
| LPG                | 000' tonnes | 15.9    | 18.3    | 20.8    | -13.1%                    | -23.6%                    |
| Heavy fuel oil     | 000' tonnes | 202.9   | 245.5   | 171.9   | -17.4%                    | 18.0%                     |
| Bunker fuel        | 000' tonnes | 8.1     | 11.2    | 6.5     | -27.7%                    | 24.6%                     |
| Bitumen components | 000' tonnes | 337.3   | 276.8   | 334.9   | 21.9%                     | 0.7%                      |
| Other              | 000' tonnes | 225.7   | 212.0   | 186.1   | 6.5%                      | 21.3%                     |

**Higher production and sales volumes in Q3 2011**

**Table 7: Sales structure of the downstream segment**

|   |             | Q3 2011 | Q2 2011 | Q3 2010 | Q3 2011<br>vs.<br>Q2 2011 | Q3 2011<br>vs.<br>Q3 2010 |
|---|-------------|---------|---------|---------|---------------------------|---------------------------|
| Consolidated sales of refining products, goods for resale and materials | 000' tonnes | 2,554.4 | 2,354.6 | 2,327.9 | 8.5%                      | 9.7%                      |
| Gasolines   | 000' tonnes | 388.9   | 369.3   | 386.1   | 5.3%                      | 0.7%                      |
| Raw gasoline  | 000' tonnes | 24.5    | 23.5    | 31.3    | 4.3%                      | -21.7%                    |
| Diesel oils   | 000' tonnes | 1,260.7 | 1,164.9 | 1,133.1 | 8.2%                      | 11.3%                     |
| Light fuel oil  | 000' tonnes | 73.5    | 66.8    | 78.6    | 10.0%                     | -6.5%                     |
| Heavy fuel oil  | 000' tonnes | 149.7   | 182.5   | 133.5   | -18.0%                    | 12.1%                     |
| JET aviation fuel   | 000' tonnes | 139.2   | 112.8   | 68.2    | 23.4%                     | 104.1%                    |
| Bitumens  | 000' tonnes | 346.9   | 271.2   | 334.1   | 27.9%                     | 3.8%                      |
| Other petroleum products  | 000' tonnes | 171.0   | 163.6   | 163.0   | 4.5%                      | 4.9%                      |

In Q3 2011, the overall production and sales volumes were higher both year on year and quarter on quarter. The increase was the highest in diesel oils and jet fuels.

**Table 10: Operating results of the downstream segment**

|                               |             | Q3 2011 | Q2 2011 | Q3 2010 | Q3 2011<br>vs.<br>Q2 2011 | Q3 2011<br>vs.<br>Q3 2010 |
|-------------------------------|-------------|---------|---------|---------|---------------------------|---------------------------|
| Sales revenue                 | <i>PLNm</i> | 7,544.6 | 6,723.1 | 5,286.4 | 12.2%                     | 42.7%                     |
| Operating profit/(loss)       | <i>PLNm</i> | 55.6    | 263.3   | 293.5   | -78.9%                    | -81.1%                    |
| Depreciation and amortisation | <i>PLNm</i> | 132.2   | 118.1   | 85.5    | 11.9%                     | 54.6%                     |
| EBITDA                        | <i>PLNm</i> | 187.8   | 381.4   | 379.0   | -50.8%                    | -50.4%                    |

The 42.7% rise in the downstream segment's sales revenue in Q3 2011 relative to Q3 2010 was mostly due to growing prices of crude oil and petroleum products on the global markets and a 9.7% higher sales volume. In Q3 2011, the average price of Brent crude (Dated Brent) was 113.41 USD/bbl, up by 36.55 USD/bbl, or 47.6%, year on year. The average net selling price in the downstream segment rose by 30.1%, from 2,271 PLN/t in Q3 2010 to 2,954 PLN/t in Q3 2011. Compared with the previous quarter, selling prices in this segment rose by 3.5%, mainly on the back of changes in the foreign exchange rate. 8.5% higher sales volume and appreciation of the US dollar against the zloty were the main reasons behind the 12.2% sales revenue increase relative to Q2 2011.

Considerable depreciation of the zloty in Q3 2011, from 2.73 PLN/USD on July 1st 2011 to 3.26 PLN/USD on September 30 2011, led to foreign exchange losses related to operating activities of PLN -282.7m in Q3 2011, while in Q3 2010 appreciation of the zloty resulted in foreign exchange gains on operating activity of PLN 70.0m. Strongly negative foreign exchange differences were the main reason driving the operating result down by PLN 237.9m relative to the comparative period. Operating result in Q3 2011 was positively affected by 226.5 thousand tonnes, or 9.7%, higher sales volume and by the sales structure. The sales volume increase was partly attributable to 163.5 thousand tonnes higher volume of crude oil processed by the Gdańsk refinery. Operating performance of the LOTOS Group was also improved by higher crack margins on fuels.

**Table 8: Number of service stations in the LOTOS network at end of period**

|      | Sep 30 2011 | Jun 30 2011 | Sep 30 2010 | Q3 2011<br>vs.<br>Q2 2011 | Q3 2011<br>vs.<br>Q3 2010 |
|------|-------------|-------------|-------------|---------------------------|---------------------------|
|      | <b>324</b>  | <b>318</b>  | <b>317</b>  | 1.9%                      | 2.2%                      |
| CODO | 161         | 158         | 153         | 1.9%                      | 5.2%                      |
| DOFO | 117         | 112         | 102         | 4.5%                      | 14.7%                     |

|                             |     |     |     |       |        |
|-----------------------------|-----|-----|-----|-------|--------|
| franchise agreements signed | 121 | 116 | 109 | 4.3%  | 11.0%  |
| DODO                        | 46  | 48  | 62  | -4.2% | -25.8% |

**Table 9: Operating results of the retail business (CODO, DOFO, DODO, SDS) \***

|                               |                 | Q3 2011 | Q2 2011 | Q3 2010 | Q3 2011 vs. Q2 2011 | Q3 2011 vs. Q3 2010 |
|-------------------------------|-----------------|---------|---------|---------|---------------------|---------------------|
| Sales volume                  | thousand tonnes | 280.6   | 264.5   | 272.9   | 6.1%                | 2.8%                |
| Sales revenue                 | PLNm            | 1,439.7 | 1,323.1 | 1,162.8 | 8.8%                | 23.8%               |
| Operating profit/(loss)       | PLNm            | -2.1    | -12.3   | 12.3    | -                   | -                   |
| Depreciation and amortisation | PLNm            | 12.0    | 11.9    | 12.3    | 0.8%                | -2.4%               |
| EBITDA                        | PLNm            | 9.9     | -0.4    | 24.6    | -                   | -59.8%              |

\*In order to better reflect the results of the Group's operations, starting from the Q4 2010 report, retail sales have been reclassified: only sales on the retail market through the CODO (including the Motorway Service Areas), DOFO, DODO and SDS (operated by LOTOS Paliwa) service station networks have been classified as retail sales. Data for the retail business relating to Q3 2010 has been restated to ensure comparability. Comparative data for other periods is available at the corporate website of Grupa LOTOS S.A.

The increase in the retail sales volumes in Q3 2011 by 6.1% relative to Q2 2011 and by 2.8% relative to the corresponding period of was mainly attributable to higher number of services stations and seasonal tendencies.

The continued negative operating performance of the retail segment is a consequence of a low unit margin on sales of fuels, especially at CODO and DOFO stations, which in turn follows from a deterioration of market conditions due to oil price rallies, with limited scope for passing the increase onto customers. Better operating result of the retail business in Q3 2011 relative to the previous quarter is partly attributable to sales seasonality.

**Table 11: Effect of inventory valuation on the operating results of the downstream segment**

|                              |      | Q3 2011 | Q2 2011 | Q3 2010 |
|------------------------------|------|---------|---------|---------|
| Operating profit/(loss)      | PLNm | 55.6    | 263.3   | 293.5   |
| LIFO effect*                 | PLNm | -124.5  | -240.1  | 81.7    |
| LIFO operating profit/(loss) | PLNm | -68.9   | 23.2    | 375.2   |

\* In line with its inventory valuation policies, the LOTOS Group uses the weighted average method to measure decrease in inventories. This method of inventory valuation defers the impact of changes in oil prices on the prices of finished products. Thus, an increase in oil prices has a positive effect on the financial performance, while a decrease drives it down. The operating result accounting for the impact of this valuation method is presented in the table.

In Q3 2011, the weighted average method of inventory valuation applied by the LOTOS Group, combined with the appreciation of the dollar in Q3 2011, drove up the operating result of the downstream segment by PLN 124.5m. In the comparative period, the inventory valuation method had a negative effect of PLN 81.7m on the operating result. In the previous quarter, i.e. Q2 2011, the operating result was lifted by PLN 240.1m. If the LIFO method had been applied to inventory valuation, the operating result of the downstream segment would have been PLN -68.9m in Q3 2011, PLN 23.2m in Q2 2011 and PLN 375.2m in Q3 2010.

**Increase in the number of services stations to 324**

**Lifo effect of PLN -124.5m**

## 4 Other business

**Table 12. Operating results of other business\***

|                               |      | Q3 2011 | Q2 2011 | Q3 2010 | Q3 2011<br>vs.<br>Q2 2011 | Q3 2011<br>vs.<br>Q3 2010 |
|-------------------------------|------|---------|---------|---------|---------------------------|---------------------------|
| Sales revenue                 | PLNm | 5.2     | 5.6     | 4.4     | -7.1%                     | 18.2%                     |
| Operating profit/(loss)       | PLNm | -0.6    | 1.1     | -0.1    | -                         | -                         |
| Depreciation and amortisation | PLNm | 2.5     | 2.5     | 2.3     | 0.0%                      | 8.7%                      |
| EBITDA                        | PLNm | 1.9     | 3.6     | 2.2     | -47.2%                    | -13.6%                    |

\* Includes: LOTOS Ekoenergia Sp. z o.o., LOTOS Park Technologiczny Sp. z o.o., Energobaltic Sp. z o.o. and LOTOS Gaz S.A. w likwidacji (in liquidation).

## 5 Statement of comprehensive income

In Q3 2011, the LOTOS Group posted PLN 92.6m in operating profit, which represented a year-on-year deterioration of 72.1% and a decrease of 71.2% on Q2 2011.

For the first nine months of 2011, operating profit of the LOTOS Group amounted to PLN 826.3m, up by PLN 69.7m on the first nine months of 2010.

**Table 13. Operating results of the LOTOS Group**

|                              |      | Q3 2011 | Q2 2011 | Q3 2010 | Q3 2011<br>vs.<br>Q2 2011 | Q3 2011<br>vs.<br>Q3 2010 |
|------------------------------|------|---------|---------|---------|---------------------------|---------------------------|
| Sales revenue                | PLNm | 7,597.5 | 6,781.4 | 5,279.7 | 12.0%                     | 43.9%                     |
| EBITDA                       | PLNm | 254.5   | 466.8   | 434.6   | -45.5%                    | -41.4%                    |
| Operating profit/(loss)      | PLNm | 92.6    | 321.1   | 332.3   | -71.2%                    | -72.1%                    |
| LIFO operating profit/(loss) | PLNm | -31.9   | 81.0    | 414.0   | -                         | -                         |

\* Starting from January 1st 2011, the Group changed its accounting policies as regards the exchange rates used to translate business transactions denominated in foreign currencies. Application of the new accounting policies did not affect the Group's total net result, but did affect the values presented in the operating and financial parts of the statement of comprehensive income. To ensure data comparability, the same policies were applied to all presented periods.

In Q3 2011, net loss from continuing operations amounted to PLN -328.6m against PLN 1,051.4m of net profit from continuing operations in Q3 2010 and PLN 253.5m of net profit in Q2 2011. Net profit from continuing operations for the nine months ended September 30th 2011 was PLN 560.4m, representing an increase of PLN 130.5m year on year.

**Table 14. Net profit of the LOTOS Group**

|  |      | Q3 2011 | Q2 2011 | Q3 2010 |
|--|------|---------|---------|---------|
| Pre-tax profit   | PLNm | -432.5  | 301.2   | 1,298.7 |
| Net profit/(loss) from continuing operations           | PLNm | -328.6  | 253.5   | 1,051.4 |
| Net profit/(loss) attributable to owners of the Parent | PLNm | -328.6  | 253.4   | 1,051.0 |

**EBITDA of  
PLN 254.5m in  
Q3 2011**

**EBIT of  
PLN 92.6m  
in Q3 2011**

**Net loss of  
PLN -328.6m in  
Q3 2011**



Differences between the net results in the presented periods are attributable to the net finance income or expenses generated by the LOTOS Group. In Q3 2011, the Group generated net finance expenses of PLN -525.1m. In Q2 2011, it reported net finance expenses of PLN -19.9m, whereas in Q3 2010 it generated a high net finance income of PLN 966.4m. In Q3 2011, depreciation of the złoty resulted in revaluation of the foreign currency denominated debt. In Q3 2011, the effect of foreign exchange differences on revaluation of loans and borrowings was PLN -363.4m and related mainly to loans of the Parent Undertaking.

Starting from January 1st 2011, Grupa LOTOS S.A. introduced cash flow hedge accounting with respect to foreign-currency denominated loans intended for financing of the 10+ Programme, designated as hedges of future USD-denominated petroleum product sales transactions. In consequence, in the period from January 1st to 30th 2011, foreign exchange losses taken to the cash flow hedging reserve were PLN -337.0m. In Q3 2011, foreign exchange losses reducing the value of the cash flow hedging reserve were PLN -585.9m.

In the analysed period, net valuation and settlement of market risk hedging transactions at the LOTOS Group was negative at PLN -130.8m.

In Q3 2011, total net loss on settlement and valuation of derivative instruments, including forwards hedging the foreign exchange risk and futures hedging the risk of changes in prices of CO<sub>2</sub> emission allowances, amounted to PLN -77.6m. The net loss on settlement and valuation of interest rate hedging transactions was PLN -57.2m. The effect of settlement and valuation of transactions hedging petroleum product prices in Q3 2011 was PLN 4.0m.

**Net finance expenses of PLN -525.1m in Q3 2011**

**Table 15: Transactions executed to hedge the risk of changes in prices of petroleum products, as at September 30th 2011**

| Period  | Product/commodity    | Light fuel oil                  |  | Heavy fuel oil               |
|---------|----------------------|---------------------------------|--|------------------------------|
|         |                      | Gasoil .1 Cargoes CIF NWE / ARA |  | 3.5 PCT Barges FOB Rotterdam |
| Q4 2011 | Volume (mt)          | -4,880                          |  | 22,180                       |
|         | Price range (USD/mt) | 715.00 - 796.25                 |  | 473.00 - 517.75              |

**Table 16: Foreign exchange risk hedging transactions as at September 30th 2011**

| Currency pair          | Instrument | Volume       | Currency | FX rate range     |
|------------------------|------------|--------------|----------|-------------------|
| EUR/USD exchange rate  | Forward    | 157,400,000  | EUR      | 1.31293 - 1.44393 |
| EUR/PLN exchange rates | Forward    | 38,000,000   | EUR      | 3.9748 - 4.2133   |
| USD/PLN exchange rates | Forward    | -110,500,000 | USD      | 2.7435 - 3.3398   |

**Table 17: Interest rate risk hedging transactions as at September 30th 2011**

| Instrument | Start date                           | End date                         | Notional amount | Currency | Interest rate range | Reference rate |
|------------|--------------------------------------|----------------------------------|-----------------|----------|---------------------|----------------|
| IRS        | from Oct 15 2008<br>from Jul 15 2011 | to Jan 15 2013<br>to Jan 15 2018 | 500,000,000     | USD      | 3.33% - 4.22%       | 6M LIBOR       |

## 6 Consolidated statement of financial position

**Table 18: Consolidated statement of financial position**

|   |             | Sep 30 2011     | Dec 31 2010     | Change         | %            |
|---|-------------|-----------------|-----------------|----------------|--------------|
| <b>Assets</b>   | <b>PLNm</b> | <b>20,391.0</b> | <b>17,727.4</b> | <b>2,663.6</b> | <b>15.0%</b> |
| Non-current assets, including:                        | PLNm        | 11,490.6        | 10,872.1        | 618.5          | 5.7%         |
| Property, plant and equipment                         | PLNm        | 9,017.5         | 6,173.8         | 2,843.7        | 46.1%        |
| Tangible assets under construction                    | PLNm        | 1,655.0         | 4,213.7         | -2,558.7       | -60.7%       |
| Current assets, including:                            | PLNm        | 8,782.2         | 6,847.4         | 1,934.8        | 28.3%        |
| Inventories   | PLNm        | 5,766.2         | 4,506.8         | 1,259.4        | 27.9%        |
| Trade and other receivables                           | PLNm        | 2,322.6         | 1,821.9         | 500.7          | 27.5%        |
| Current financial assets                              | PLNm        | 136.9           | 55.9            | 81.0           | 144.9%       |
| Cash and cash equivalents                             | PLNm        | 390.1           | 382.6           | 7.5            | 2.0%         |
| Assets available for sale                             | PLNm        | 118.2           | 7.9             | 110.3          | 1396.2%      |
| <b>Equity and liabilities</b>                         | <b>PLNm</b> | <b>20,391.0</b> | <b>17,727.4</b> | <b>2,663.6</b> | <b>15.0%</b> |
| Equity  | PLNm        | 7,829.9         | 7,513.5         | 316.4          | 4.2%         |
| Non-current liabilities                               | PLNm        | 7,078.1         | 5,039.1         | 2,039.0        | 40.5%        |
| Current liabilities                                   | PLNm        | 5,431.6         | 5,174.6         | 257.0          | 5.0%         |
| Liabilities associated with assets available for sale | PLNm        | 51.4            | 0.2             | 51.2           | 25,600.0%    |

As at September 30th 2011, the LOTOS Group had total assets of PLN 20,391.0m, which means an increase of PLN 2,663.6m during the first nine months of 2011. Non-current assets grew by PLN 618.5m, mainly due to the recognition of intangible assets in the amount of PLN 291.8m, representing licences awarded to AB Geonafra and its group members (UAB Genciu Nafta, UAB Minijos Nafta, and UAB Manifoldas) which confer the right to exploit crude oil reserves in Lithuania, as well as due to the PLN 285.0m increase in property, plant and equipment (including tangible assets under construction) relating mainly to the expenditure made in the upstream segment.

As at September 30th 2011, inventories amounted to PLN 5,766.2m, having increased over the first nine months of 2011 by PLN 1,259.4m, mainly due to higher volumes of mandatory stocks and higher prices of crude oil and petroleum products as at the end of Q3 2011 relative to the end of 2010. Higher product prices also brought about a PLN 500.7m rise in trade and other receivables. At the end of September 2011, current assets totalled PLN 8,782.2m, and were higher by PLN 1,934.8m relative to the end of 2010.

As at September 30th 2011, equity amounted to PLN 7,829.9m, having grown by PLN 316.4m over the first nine months of 2011, primarily as a result of the PLN 565.3m increase in retained earnings and the PLN 273.0m foreign exchange losses on valuation of cash flow hedges net of the tax effect, taken to the cash flow hedging reserve.

In the first nine months of 2011, non-current liabilities went up by PLN 2,039.0m, mostly on the back of a PLN 1,908.3m increase in non-current interest-bearing loans and borrowings. In Q3 2011, debt related to inventory financing was reclassified from current to non-current, in connection with the agreement of August 2011 which extended the term of the inventory financing facility by another 12 months.

At the end of September 2011, current liabilities stood at PLN 5,431.6m, having grown by PLN 257.0m in 2011, mainly due to a PLN 1,093.0m increase in trade payables, accruals and deferred income and other liabilities, following primarily from a 27.7% increase in the value of crude oil purchased in September 2011 compared with the crude oil purchased in December 2010. Concurrently, current loans and borrowings decreased by PLN 924.8m, mostly as a result of the agreement extending the term of the inventory financing facility.

As at September 30th 2011, financial debt of the LOTOS Group amounted to PLN 7,310.3m, having increased by PLN 983.5m from the figure reported at the end of 2010, chiefly on the back of changes in the USD/PLN exchange rate. The ratio of financial debt (adjusted by free cash) to equity was 88.4%, i.e. by 9.3pp more than as at December 31st 2010.

**Financial debt of  
PLN 7,310.3m at  
the end of Q3  
2011**

## 7 Consolidated statement of cash flows

**Table 19: Consolidated statement of cash flows**

|  |             | Q3<br>2011 | Q2<br>2011 | Q3<br>2010 |
|--|-------------|------------|------------|------------|
| Cash flows from operating activities             | <i>PLNm</i> | 473.8      | -588.1     | 357.5      |
| Cash flows from investing activities             | <i>PLNm</i> | -188.9     | -175.8     | -275.2     |
| Cash flows from financing activities             | <i>PLNm</i> | -29.2      | 4.2        | 213.1      |
| Change in net cash                               | <i>PLNm</i> | 279.0      | -760.5     | 288.6      |
| Cash and cash equivalents at beginning of period | <i>PLNm</i> | -266.3     | 494.2      | -81.5      |
| Cash and cash equivalents at end of period       | <i>PLNm</i> | 12.7       | -266.3     | 207.1      |

As at the end of Q3 2011, the LOTOS Group's cash balance (including current account overdrafts) was PLN 12.7m, and was by PLN 194.4m lower than at the end of Q3 2010, but by PLN 279.0m higher than at the end of Q2 2011.

The PLN 473.8m positive balance of cash flows from operating activities reported in Q3 2011 is related chiefly to the PLN 766.3m increase in current liabilities excluding loans and borrowings. The PLN -588.1m negative balance reported in the previous quarter was mainly attributable to the increase in mandatory stocks.

In the discussed period, PLN 86.3m higher negative cash flows from investing activities relative to the comparable period were chiefly attributable to lower expenses incurred to acquire property, plant and equipment and intangible assets.

In Q3 2011, the balance of cash flows from financing activities was negative at PLN -29.2m. The figure accounts for PLN -155.2m of repayment of loans and borrowings along with interest paid, adjusted by increase in loans and borrowings, a PLN 99.0m net bonds issue and redemption figure and PLN 29.1m of positive settlement of financial instruments.

**Cash flows from operating activities of PLN 473.8m in Q3 2011**